

Updated Informative Digest for
Adoption of Proposed Amendments to California Code of Regulations,
Title 18, Section 133, *Business Inventory Exemption*

On May 22, 2014, the State Board of Equalization (Board) held a public hearing on and unanimously voted to adopt the original text of the proposed amendments to California Code of Regulations, title 18, section (Property Tax Rule) 133, *Business Inventory Exemption*, described in the notice of proposed regulatory action. There have not been any changes to the applicable laws or the effects and objectives of the adoption of the proposed amendments to Property Tax Rule 133 described in the informative digest included in the notice of proposed regulatory action.

The Board received public comments in support of the proposed amendments, which are consistent with the factual basis for the proposed amendments provided in the informative digest included in the notice of proposed regulatory action and discussed in more detail below. The Legislature enacted and the Governor signed Assembly Bill No. (AB) 777 (Stats. 2014, ch. 13.), which is discussed in the informative digest included in the notice of proposed regulatory action and discussed further below. The Board received objections to the proposed amendments from the Los Angeles County Assessor's Office (LACAO) and Mr. Lawrence E. Stone, the Santa Clara County Assessor, which are summarized and responded to below. The Board also added to the anticipated benefits described in the informative digest included in the notice of proposed regulatory action, as provided below.

The informative digest included in the notice of proposed regulatory action provides:

Current Law

California Constitution, article XIII, section 1 provides that, unless otherwise provided by the California Constitution or by the laws of the United States, all property is taxable. All property includes tangible personal property. However, RTC section 219 provides that, "For the 1980-81 fiscal year and fiscal years thereafter, business inventories are exempt from taxation and the assessor shall not assess business inventories."

Under Government Code section 15606, subdivision (c), the State Board of Equalization (Board) is authorized to prescribe rules and regulations to govern local boards of equalization and assessment appeals boards when equalizing and county assessors when assessing. Government Code section 15606, subdivision (f) authorizes the Board to prescribe "rules, regulations, instructions, and forms relating to classifications of kinds of property and evaluation procedures." The Board adopted California Code of Regulations, title 18, section (Property Tax Rule) 133, *Business Inventory Exemption*, pursuant to Government Code section 15606, to

implement, interpret, and make specific the provisions, under article XIII of the California Constitution and the RTC, applicable to the exemption of business inventories.

In particular, Property Tax Rule 133 implements, interprets, and makes specific RTC sections 129 and 219. RTC section 129 defines “business inventories” as follows:

“Business inventories” shall include goods intended for sale or lease in the ordinary course of business and shall include raw materials and work in process with respect to such goods. “Business inventories” shall also include animals and crops held primarily for sale or lease, or animals used in the production of food or fiber and feed for such animals.

“Business inventories” shall not include any goods actually leased or rented on the lien date nor shall “business inventories” include business machinery or equipment or office furniture, machines or equipment, except when such property is held for sale or lease in the ordinary course of business. “Business inventories” shall not include any item held for lease which has been or is intended to be used by the lessor prior to or subsequent to the lease. “Business inventories” shall not include goods intended for sale or lease in the ordinary course of business which cannot be legally sold or leased in this state. If goods which cannot be legally sold or leased are not reported by the taxpayer pursuant to Section 441, it shall be conclusively presumed that the value of the goods when discovered is the value of the goods on the preceding lien date.

“Business inventories” shall also include goods held by a licensed contractor and not yet incorporated into real property.

As relevant here, subdivision (a)(1) of Property Tax Rule 133 further defines the term “business inventories” and also defines the phrases “ordinary course of business” and “goods intended for sale or lease,” as used in RTC section 129. The Board added the current provisions of subdivision (a)(2)(A), (C), and (D) to Property Tax Rule 133, in 2000, in order to provide a list of the specific types of property that the Board had previously determined are included within the meaning of the term “business inventories” prior to 2000. And, the Board added subdivision (a)(2)(B) to Property Tax Rule 133, in 2000, to clarify that the Board had recently determined that new and used oak barrels are business inventories, under specific circumstances.

Effects, Objectives, and Benefits of the Proposed Amendments

The transfer of control of space flight property to the federal government is required by Air Force Space Command (AFSPC). Authority over space

flight property launch is granted to the Air Force via the Commercial Space Launch Act of 1984, as amended in 1988 (49 U.S.C. §§ 2601-23, October 30, 1984) which grants regulatory authority over space flight property to the Department of Transportation, which through the Federal Aviation Administration Office for Commercial Space Transportation entered into an agreement with the United States Air Force regarding the implementation of procedures for commercial space transportation and range activities. (See Memorandum of Agreement Between Department of the Air Force and Federal Aviation Administration on Safety for Space Transportation and Range Activities, at https://www.faa.gov/about/office_org/headquarters_offices/ast/media/moa.pdf (as of March 18, 2014).)

AFSPC directs safety requirements for both range users and air force space command organizations and requires that control over space flight property be transferred to a federal launch safety authority for flight termination purposes upon launch. (Chapters 6 and 7 of Launch Safety Requirements for Air Force Space Command Organizations, Air Force Space Command Manual 91-711 (February 1, 2007) (AFSPC Manual 91-711) provide mission flight control officers with power to issue flight termination commands.)

The federal launch safety authority, in its sole discretion, may terminate the flight. (AFSPC Manual 91-711, § 7.1.1.1.) Termination of the flight would result in destruction of the space flight property. Because the federal launch safety authority may, in its sole discretion, destroy the space flight property, all meaningful control over such property has been ceded to it.

Prior to December 2013, the Board had provided general guidance regarding the business inventory exemption and specific guidance regarding its application to various types of property; however, the previous Board guidance had not specifically discussed the application of the business inventory exemption to space flight property. By letter dated December 24, 2013, the Board's Legal Department opined that the business inventory exemption applies to space flight property fabricated and used to transport satellites and cargo to locations in outer space and over which the owner relinquishes ultimate control at launch. In the letter, the Board's Legal Department also opined that Property Tax Rule 133 should be amended to specifically address the applicability of the business inventory exemption to space flight property governed by federal statutes and regulations.

As relevant here, RTC section 129 includes as business inventory "goods intended for sale . . . in the ordinary course of business." The Property Tax Law (RTC § 50 et seq.) does not specifically define this phrase. Property Tax Rule 133, subdivision (a)(1)(A) provides, however, that,

“The phrase ‘ordinary course of business’ . . . require[s] that the property be intended for sale or lease in accordance with the regular and usual practice and method of the business of the vendor or lessor.” Due to the unique nature of the space flight industry, the determination of whether space flight property is a “good intended for sale in the ordinary course of business” must be based upon all the relevant facts and circumstances and take into account the heavy federal regulation which constrains the transfer of title of space flight property. (The Arms Export Control Act (AECA) (22 U.S.C. § 2778) authorizes the President to designate items as defense articles and defense services on the United States Munitions List (Munitions List) for purposes of promulgating regulations for the import and export of such articles (22 U.S.C. § 2278, subd. (a)(1)); and the Munitions List is contained in and regulated by the International Traffic in Arms Regulations (ITAR), which places a number of requirements on any company intending to export items on the Munitions List (22 C.F.R. §§ 120-130).) Within that context, the Board’s Legal Department determined that the transfer of control to the federal launch safety authority upon launch, for a consideration, is a “sale” and makes space flight property “goods intended for sale in the ordinary course of business” within the meaning of RTC sections 129 and 219 and Property Tax Rule 133. The Board’s Legal Department also based its determination that space flight property is business inventory, under such circumstances, on that fact that it is consistent with the Sales and Use Tax Law (RTC § 6001 et seq.) as well as case law regarding the business inventory exemption from property tax.

In determining whether property qualifies as business inventory for property tax purposes, the Board’s Legal Department found that courts have looked to whether sales tax is owed on transactions involving the property as an important factor in determining whether that property was in fact sold and intended for sale (i.e., was business inventory) prior to such sale. (See *Westinghouse Beverage Group v. County of San Diego* (1988) 203 Cal.App.3d 1442 (hereafter, *Westinghouse*) [soft drink manufacturer’s reusable containers supplied to wholesale customers held not to be business inventory where manufacturer did not collect sales tax reimbursement under Cal. Code Regs., tit. 18, § 1700]); See also *Amdahl Corporation v. County of Santa Clara* (2004) 116 Cal.App.4th 604 [sales tax reimbursement not collected on rotatable spare parts – held not business inventory].) This is because sales tax is imposed on retailers and is measured by each retailer’s gross receipts from each “retail sale,” which is defined as “a sale for any purpose other than resale in the regular course of business.” (RTC §§ 6006, 6007, and 6051.) And, it follows that if sales tax is owed on a transaction involving specified property that was entered into in the ordinary course of business, then the property was “sold” in a retail sale and that same property was necessarily, prior to sale, property that was “intended for sale in the ordinary course of business” (i.e.,

business inventory). Thus, the courts recognize that the definition of “goods intended for sale in the ordinary course of business” must have the same meaning for the same transaction, and thus the same definition is applicable to both sales and property tax. In other words, there is not one definition of inventory for sales tax purposes and a different definition of inventory for property tax purposes.

In addition, under the Sales and Use Tax Law, the term “sale” means any transfer of title to or possession of property for a consideration and the term “transfer of possession” includes those transactions found by the Board to be in lieu of a transfer of title. (RTC § 6006.) Due to the unique nature of the space flight industry, the Board’s Legal Department concluded that when a space flight property company transfers possession (control) of specified space flight property to the federal government at launch, for a consideration paid to the company by its customer, the transfer of possession is in lieu of a transfer of title. Accordingly, the transfer of space flight property to federal government control at launch, for a consideration, is a retail sale for sales tax purposes pursuant to RTC sections 6006 and 6007. And, but for the specific exemption for qualified property for use in space flight provided by RTC section 6380, space flight property companies would owe sales tax on such transfers. Therefore, since for sales tax purposes, a retail sale has taken place under such circumstances, it necessarily follows that such goods, prior to sale, were intended for sale in the ordinary course of business, requiring the classifying of such property as business inventory.

Furthermore, the classification of space flight property as business inventory is also consistent with California property tax cases considering the element of control over the property in determining whether the property qualifies for the business inventory exemption. For example, in *Westinghouse, supra*, 203 Cal.App.3d 1442, the court considered syrup and CO2 containers. It held that such containers did not qualify as inventory since the seller retained control over the containers on the lien date even though the containers were in the physical possession of its customers. The court contrasted this situation with returnable bottles in which soft drinks are sold because the bottles were not within the seller’s control once sold. In *Transworld Systems v. County of Sonoma* (2000) 78 Cal.App.4th 713, 717 (hereafter, *Transworld*), the court opined that property transferred with a nonprofessional service constituted business inventory since the goods were transferred away from the business pursuant to a customer’s direction. Implicit in this reasoning is that the customer, not the business, had control, albeit indirect, of where the goods would be delivered. Also, in *Transworld*, the court explained that “[w]hile statutes granting property tax exemptions are generally construed strictly, that approach ‘does not require that the narrowest possible meaning be given to words descriptive of the exemption, for a fair and reasonable

interpretation must be made of all laws, with due regard for the ordinary acceptance of the language employed and the object sought to be accomplished thereby. [Citations].” (*Id.* at p. 716.) Therefore, based upon the heavy federal regulation, which constrains the transfer of title to space flight property, and the above discussion of property and sales tax law, the Board’s Legal Department concluded that space flight property to which control is ceded to the federal launch safety authority, for a consideration, is property that is intended to be sold in the ordinary course of business and is properly classified as inventory. And, as inventory, such property qualifies for the business inventory exemption under the current provisions of RTC sections 129 and 219.

In Letter to Assessors (LTA) 2014/004, *Property Tax Rule 133, Business Inventory Exemption*, dated January 8, 2014, the Board’s Property and Special Taxes Department advised interested parties that a project had been initiated to proposed revisions to Property Tax Rule 133 due to “inquiries as to whether the business inventory exemption applies to certain space flight property regulated under the Arms Export Control Act (AECA) and the International Traffic in Arms Regulations (ITAR)” (footnotes omitted). The LTA also noted the Legal Department’s December 24, 2013, letter regarding space flight property (discussed above), provided a link to a redacted copy of the letter posted on the Board’s website, and gave the interested parties an opportunity to provide comments and suggestions by January 31, 2014.

Board staff conducted an interested parties meeting on February 6, 2014, to discuss the proposed revisions to Property Tax Rule 133. Staff subsequently prepared Formal Issue Paper 14-002, which included as attachments the comments received in support of and in opposition to Board staff’s proposed amendment to Property Tax Rule 133, and submitted it to the Board for consideration during its February 25, 2014, Property Tax Committee meeting.

In the formal issue paper, Board staff recommended that the Board amend Property Tax Rule 133 to add subdivision (a)[(2)](E),¹ to clarify that space flight property, not operationally reusable and the control over which is relinquished by the owner upon launch, qualifies for the business inventory exemption. The formal issue paper recommended that the Board propose to add the following language to Property Tax Rule 133, subdivision (a)[(2)]:²

¹ The informative digest in the notice of proposed regulatory action contained a typographical error which caused it to incorrectly state that Board staff recommended that the Board amend Property Tax Rule 133 to add subdivision (a)(1)(E), instead of the correct subdivision (a)(2)(E). Board staff noted the typographical error for the record during the public hearing regarding the proposed amendments to Property Tax Rule 133 on May 22, 2014.

² See footnote 1.

(E) Space flight property, not operationally reusable, listed in the International Traffic in Arms Regulations on the United States Munitions List (22 CFR § 121.1), the control over which is relinquished by the owner upon launch.

(i) “Space flight” means any flight designed for suborbital, orbital, or interplanetary travel.

(ii) The phrase “control over which is relinquished by the owner upon launch” means the transfer of control to a federal launch safety authority for space flight termination purposes.

In addition, in the formal issue paper, Board staff summarized the comments in support of and in opposition to its proposed amendments to Property Tax Rule 133. Board staff responded to the comments in opposition. Board staff also specifically explained that the proposed amendments clarifying the definition of “business inventories” will not apply to “reusable” space flight property. Board staff specifically explained that its proposed amendments are “very narrowly tailored to interpret [RTC] sections 129 and 219 to include as business inventory only spaceflight property regulated by federal statutes and regulations and for which control is relinquished upon launch.” Board staff specifically explained that the proposed amendments are more limited than the exemption afforded by Assembly Bill No. (AB) 777 (2013-2014 Reg. Sess.) because Property Tax Rule 133 only applies to business inventory, while AB 777 would exempt all spaceflight property whether inventory or not. And, Board staff specifically explained that “[because the issue of the qualification of space flight property as exempt business inventory is one that has potential statewide significance and is interpretative of and consistent with existing statutes, it is the proper subject of rulemaking.”

At the conclusion of the Board’s discussion of Formal Issue Paper 14-002 during the February 25, 2014, Property Tax Committee meeting, the Board determined that Property Tax Rule 133 does not address the application of the business inventory exemption to space flight property, and that it is necessary to amend Property Tax Rule 133, as recommended by staff, to have the effect and accomplish the objective of addressing the application of the business inventory exemption to space flight property. Therefore, the Board agreed with staff’s recommendation and the Board Members unanimously voted to propose the amendments to Property Tax Rule 133 recommended by staff, and requested that staff provide additional clarification regarding the “ceding of control” and additional analysis of the federal authority regarding the transfer of control, which is provided above and in the initial statement of reasons.

The Board anticipates that the proposed amendments to Property Tax Rule 133 will promote fairness and benefit taxpayers, Board staff, and the Board, by clarifying that RTC sections 129 and 219 apply to non-reusable space flight property, the control over which is relinquished by the owner upon launch.

The Board has performed an evaluation of whether the proposed amendments to Property Tax Rule 133 are inconsistent or incompatible with existing state regulations. The Board has determined that the proposed amendments are not inconsistent or incompatible with existing state regulations because Property Tax Rule 133 is the only regulation implementing RTC sections 129 and 219, and the proposed amendments make Property Tax Rule 133 consistent with the statutes as discussed above. In addition, the Board has determined that there are no comparable federal regulations or statutes to Property Tax Rule 133 or the proposed amendments to Property Tax Rule 133.

Public Comments in Support of the Proposed Amendments

The Board received written comments from Mr. Mardiros H. Dakessian, on behalf of Space Exploration Technologies Corporation (SpaceX), by letter dated May 19, 2014, expressing support for the adoption of the Board's proposed amendments to Property Tax Rule 133, and responding to comments from Mr. Stone's letter dated April 9, 2014 (discussed below). In his letter, Mr. Dakessian agrees that it is necessary to adopt the proposed amendments to Property Tax Rule 133 to clarify how existing law applies to space flight property. Mr. Dakessian agrees with the Board's analysis "with respect to the responsibilities and authority of the Air Force (Range Safety) and the Mission Flight Control Officer's role as the sole decision-making authority and initiator of the flight termination system." Mr. Dakessian explains that a SpaceX vehicle is "preprogrammed and autonomous and the Range User (such as SpaceX) has no ability to control the vehicle from launch to reaching orbital space." Mr. Dakessian also explains that because "the Range User has no ability to control the vehicle from launch to reaching orbital space," the "Range Safety control for safety purposes is in fact the *only* control that exists during the mission [and] . . . range safety is of paramount importance to any launch. Ceding control to federal authorities is required by the federal system to ensure public safety and cannot be minimized." (Emphasis in original.)

The Board also received written comments from Mr. David Flaks, on behalf of the Los Angeles County Economic Development Corporation (LAEDC), by letter dated May 19, 2014, offering support for the Board's proposed amendments to Property Tax Rule 133 because they are rational, objectively fair, and provide for equitable treatment of businesses in California.

In addition, Ms. Debra Reynolds Clark appeared at the public hearing on behalf of United Launch Alliance (ULA) and expressed support for the adoption of the Board's proposed amendments to Property Tax Rule 133. Ms. Reynolds Clark stated that ULA, Boeing,

and Lockheed have been subject to property tax audits over the past 15 years, for which rockets have always been treated as business inventory by county assessors. (Transcript of May 22, 2014, public hearing, p. 16, lines 26-28, and p. 17, lines 1-3.) Further, in her oral testimony, Ms. Reynolds Clark restated the factual basis for the proposed amendments to Property Tax Rule 133, as provided in the informative digest (and quoted above). Ms. Reynolds Clark emphasized that the launch vehicles at issue are 100 percent non-reusable. (Transcript of May 22, 2014, public hearing, p. 17, lines 9-16.) Further, to emphasize that commercial space flight companies completely relinquish control over the space flight property upon launch, Ms. Reynolds Clark reiterated that at the Vandenberg Air Force Base, the range safety officer of the federal government takes control over the rocket even before take-off. The range safety officer has the authority to destroy the vehicle on the launch pad, as well as during flight, for safety reasons. Even during flight, the commercial space flight companies have no control over the course of the vehicle, because directives to steer and deliver its payload are programmed prior to launch. (Transcript of May 22, 2014, public hearing, p. 17, lines 17-28, and p. 18, lines 1-24.) Ms. Reynolds Clark also emphasized that, in her opinion, “being able to destroy a rocket is the ultimate sign of ownership [and] . . . ultimate sign of control.” (Transcript of May 22, 2014, public hearing, p. 18, lines 5-7.)

Furthermore, Mr. Dennis Loper appeared at the public hearing, on behalf of SpaceX, and expressed support for the proposed amendments to Property Tax Rule 133, emphasizing that the space flight property at issue is not currently reusable. Also, Mr. Dakessian appeared at the public hearing, on behalf of SpaceX, and expressed support for the adoption of the proposed amendments to Property Tax Rule 133. Mr. Dakessian reiterated Ms. Reynolds Clark’s testimony that all meaningful control of space flight property is relinquished to the range safety officer prior to and upon launch. Mr. Dakessian also responded to Mr. Albert Ramseyer’s testimony (discussed below) by stating that SpaceX is in fact a manufacturer.

AB 777

When the Board initially voted to propose to adopt the amendments to Property Tax Rule 133, the Board was aware that the Legislature was considering enacting AB 777 to add section 242 to the Revenue and Taxation Code (RTC) to provide a property tax exemption for “qualified property used in space flight.” The informative digest (quoted above) explained that the proposed amendments to Property Tax Rule 133 are more limited than the exemption afforded by AB 777 “because Property Tax Rule 133 only applies to business inventory, while AB 777 would exempt all space flight property whether inventory or not.”

Since the publication of the notice of proposed regulatory action for the proposed amendments to Property Tax Rule 133, the Legislature enacted and the Governor signed AB 777. As a result, RTC section 242 now provides a property tax exemption for “qualified property for use in space flight.” However, RTC section 242, subdivisions (d) and (g), provide that RTC section 242 is only operative from the January 1, 2014, lien date to, and including, the January 1, 2024, lien date, and section 242 is repealed by its

own terms effective July 1, 2025. Furthermore, in section 6 of AB 777, the legislature explicitly stated that:

An inference shall not be drawn from this act with respect to whether space flight property qualifies as “business inventories” as defined or described by Sections 129 and 219 of the Revenue and Taxation Code, or Board of Equalization Property Tax Rule 133.

Summary of and Responses to Objections to the Proposed Amendments

The Board received written objections regarding the proposed amendments to Property Tax Rule 133 from Mr. Lawrence E. Stone, Santa Clara County Assessor, via a letter dated April 9, 2014. In his letter, Mr. Stone opposed amending Property Tax Rule 133 to clarify that space flight property, not operationally reusable and the control over which is relinquished by the owner upon launch, qualifies for the business inventory exemption. This is because, in his opinion, there is always an insufficient ceding of control of the space flight property to a range safety officer. However, as stated in the informative digest and as explained further above, because the federal launch safety authority receives sufficient control, so that it may, in its sole discretion, destroy the space flight property due to safety concerns, the Board has determined that all meaningful control over such property is in fact ceded to the federal launch safety authority. This determination is further supported by the written comments from Mr. Dakessian and the testimony from Ms. Reynolds Clark (discussed above), which indicate that commercial space flight companies relinquish control of their space flight vehicles prior to launch and have no control over the pre-programmed course of their space flight vehicles in flight.

Mr. Stone further states in his April, 8, 2014, letter that he opposes the proposed amendments to Property Tax Rule 133 because, in his opinion, the amendments would preclude the assessment of reusable, or potentially reusable, space flight property. However, this statement is inconsistent with the plain language of the proposed amendments to Property Tax Rule 133, which state explicitly that the business inventory exemption applies to spaceflight property that is “not operationally reusable.”

The Board also received written comments from John F. Krattli, County Counsel for the LACAO, via a letter dated May 20, 2014. In the letter, Mr. Krattli opposed amending Property Tax Rule 133, stating that: (1) there is no need for the Board to clarify the application of the business inventory exemption to space flight property because the clarification would only apply retroactively after the enactment of RTC section 242; (2) the Board does not have authority to adopt the proposed amendments because Property Tax Rule 133 did not previously address space flight property; and (3) it is for the legislature to decide whether to exempt property from assessment.

However, as indicated above, RTC section 242, subdivision (d), expressly provides that RTC section 242 only applies from the “January 1, 2014, lien date to, and including, the January 1, 2024, lien date, and is inoperative for any lien date thereafter.” Therefore, the exemption for qualified property for use in space flight provided by RTC section 242 will

no longer apply after January 1, 2024, and such property may be subject to assessment, on a prospective basis, unless the business inventory exemption applies. As a result, there is still a need to clarify whether the business inventory exemption applies to space flight property, on a prospective basis, after the addition of section 242 to the RTC.

In addition, as indicated above, the Legislature has stated that the enactment of RTC section 242 is not intended to create any “inference” as to whether space flight property qualifies as business inventory. Also, Government Code section 15606, subdivision (c), authorizes the Board to prescribe rules and regulations to govern local boards of equalization and assessment appeals boards when equalizing and county assessors when assessing. Government Code section 15606, subdivision (f), authorizes the Board to prescribe “rules, regulations, instructions, and forms relating to classifications of kinds of property and evaluation procedures.” As stated in the informative digest, the Board has previously made substantive amendments to Property Tax Rule 133 regarding the qualification of specific property, including clarifying in 2002 that oak wine barrels used in the wine manufacturing process qualify for the business inventory exemption. Therefore, the Board does have the authority to amend Property Tax Rule 133 to address the application of the business inventory exemption to specific types of property, and the Legislature has not expressed any intent to preempt or supersede that authority with regard to the application of the business inventory exemption to space flight property.

In his letter, Mr. Krattli further argues that the proposed amendments to Property Tax Rule 133 are substantively wrong because, in his opinion, the true object of the contracts to provide space flight property is a service, the service providers (as he characterizes them) merely contract with the government for use of its range safety systems, and there is no sale of space flight property because the customer never takes delivery of the property.

However, the Board disagrees and has concluded that the information provided in the informative digest and the comments in support of the proposed amendments more fairly support the determination that there is a sale when a provider of space flight property relinquishes possession (control) of that property to a third party, for a consideration. As stated in the informative digest, due to the unique nature of the space flight industry, the Board’s Legal Department concluded that when a space flight property company transfers possession (control) of specified space flight property to the federal government at launch, for a consideration paid to the company by its customer, the transfer of possession is in lieu of a transfer of title. Accordingly, the transfer of space flight property to federal government control at launch, for a consideration, is a retail sale for sales tax purposes pursuant to RTC sections 6006 and 6007. Since for sales tax purposes, a retail sale has taken place under such circumstances, it necessarily follows that such goods, prior to sale, were intended for sale in the ordinary course of business, requiring the classifying of such property as business inventory.

On May 22, 2014, the Board held a public hearing regarding the adoption of the proposed amendments to Property Tax Rule 133. Mr. Stone appeared at the public hearing and restated his opposition, as expressed in his written comments described above, to the

proposed amendments to Property Tax Rule 133. Mr. Stone added that Board staff has not answered the question of who owns the space vehicles after launch. He further asserted that SpaceX has indicated plans for creating reusable space vehicles, concluding that “[t]his rule would likely preclude assessing that property.” (Transcript of May 22, 2014, public hearing, p. 8, lines 16-17.)

For space flight property that returns to Earth, in some cases, ownership of the non-reusable vehicle is held by the commercial space flight company. However, as explained above, ownership of a non-reusable spaceflight vehicle after a commercial space flight company transfers possession (control) of the vehicle to the federal government at (or just prior to) launch, for a consideration paid to the company by its customer, is irrelevant; and Property Tax Rule 133 requires only that control is transferred. Further, as explicitly stated in Property Tax Rule 133 and stated in Formal Issue Paper 14-002 and in the informative digest, the proposed amendments to Property Tax Rule 133 will not apply to reusable spaceflight property. As such, to the extent that space flight property is reusable, it would not qualify for the business inventory exemption based upon the proposed amendments.

Mr. Albert Ramseyer also appeared at the public hearing on behalf of LACAO, and expressed opposition to the proposed amendments to Property Tax Rule 133, restating the written comments by Mr. Krattli that the Board does not have authority to provide an argument for the retroactive exemption of space flight property. As stated above, the proposed amendments to Property Tax Rule 133 will have a prospective application. Also, as stated above, the legislature’s statement in section 6 of AB 777, that RTC section 242 is not intended to create any “inference” as to whether space flight property qualifies as business inventory, confirms that the rulemaking authority of the Board in this respect is not superseded. Government Code section 15606, subdivision (c), authorizes the Board to prescribe rules and regulations to govern local boards of equalization and assessment appeals boards when equalizing and county assessors when assessing. Government Code section 15606, subdivision (f), authorizes the Board to prescribe “rules, regulations, instructions, and forms relating to classifications of kinds of property and evaluation procedures.” As stated in the informative digest, the Board has previously made substantive amendments to Property Tax Rule 133 regarding the qualification of specific property, including clarifying in 2002 that oak wine barrels used in the wine manufacturing process qualify for the business inventory exemption. Therefore, the Board does have the authority to amend Property Tax Rule 133 to address the application of the business inventory exemption to specific types of property, and the Legislature has not expressed any intent to preempt or supersede that authority with regard to the application of the business inventory exemption to space flight property.

At the public hearing, Mr. Ramseyer further opposed the proposed amendments to Property Tax Rule 133 because he states that they are based on the false premise that companies like ULA and SpaceX are engaging in a manufacturing business, when in fact they are a launch business. Because, in his opinion, the rockets are not built to be held for sale, but rather to provide launch services, Mr. Ramseyer asserts that they should be subject to assessment.

As in the response to the written statement from Mr. Krattli (for LACAO) described above, the Board disagrees and has concluded that the information provided in the informative digest and the comments in support of the proposed amendments more fairly support the determination that there is a sale when a provider of space flight property relinquishes possession (control) of that property to a third party, for a consideration. As stated in the informative digest, due to the unique nature of the space flight industry, the Board's Legal Department concluded that when a space flight property company transfers possession (control) of specified space flight property to the federal government at launch, for a consideration paid to the company by its customer, the transfer of possession is in lieu of a transfer of title. Accordingly, the transfer of space flight property to federal government control at launch, for a consideration, is a retail sale for sales tax purposes pursuant to RTC sections 6006 and 6007. Since for sales tax purposes, a retail sale has taken place under such circumstances, it necessarily follows that such goods, prior to sale, were intended for sale in the ordinary course of business, requiring the classifying of such property as business inventory.

No other interested parties submitted written comments regarding the proposed amendments to Property Tax Rule 133 and no other interested parties asked to speak at the public hearing.

Anticipated Benefits

In the informative digest included in the notice of proposed regulatory action (quoted above) and in the ISR, the Board indicated that it anticipates that the proposed amendments to Property Tax Rule 133 will promote fairness and benefit taxpayers, Board staff, and the Board, by clarifying that RTC sections 129 and 219 apply to non-reusable space flight property, the control over which is relinquished by the owner upon launch. In addition, the Board's proposed amendments are anticipated to provide the following benefits:

1. Give needed guidance to county assessors as to whether space flight property qualifies as "business inventory" in California; and
2. Ensure that Property Tax Rule 133 is interpreted and administered consistently with RTC sections 129 and 219.